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Source 2 introduces new concept in controlling equipment inventories

By Martha Reiner

More than 150 electronic equipment manufacturers have joined Santa Clara-based Source 2 International, a new kind of marketplace created by Robert A. Solomon, 39, and Kirk T. Jensen, 37.

This computerized electronic components exchange opened for trading this April, about half a year after Source 2 was formed.

The kind of companies that can join the exchange — original equipment manufacturers — continually have problems with excess inventory, said Solomon, president. They tend to buy in large lots to get good prices and to be prepared to fill orders efficiently.

Original equipment manufacturers buy components (or semi-finished equipment) to put in their products.

Electronic equipment designs change frequently, said Samuel F. Williams, 33, vice president for finance and administration. So manufacturers often end up with big chunks of part lots unsuited for the products they were bought for.

Also, he said, companies will sometimes overestimate the demand for a product. Again, the result is surplus parts tying up space and capital.

The equipment manufacturers can also underestimate the demand for a product, though. Then they need to locate extra parts quickly or lose potential deals by being unable to fill orders.

Traditionally, when a company has trouble unloading excess inventory through distributors or by printing up lists and trying on its own, Williams said, it will end up selling through a broker, usually getting only about 10 cents on the dollar.

Solomon: Capitalism at its best

Source 2 offices across the nation receive buyer inquiries and respond with parts' availability and pricing information

Many companies hold on to spare parts for this reason, Solomon said, hoping to use them at some point, "but the write-off is hard to take."

Source 2's alternate solution to equipment manufacturers' excess inventory problems is — for members — a call to the computerized exchange and, more than likely, a match, a deal with immediate delivery.

Parts can be listed and sold through Source 2 at 20 percent to 30 percent less than a standard distributor's price, he said.

"We make it possible for members to get cost recoveries of 50 percent to 90 percent," he said. "That's 500 percent to 900 percent of what they would get by selling to a broker."

Source 2 gets 10 percent of the final sale price from the seller if a deal is made.

When a member calls in, gives his password and requests a part, Williams said, an operator will say whether the part or a substitute is available, what the lowest selling price is, and how many are available from this source. If these suit a prospective buyer, the operator will give out the name of the selling company and the person to contact.

The operator will check with the seller the next day to see whether the deal closed and what the final price was.

"When the buyer says he's interested, the deal goes through in almost all cases," said Williams.

Source 2 is currently getting a 50 percent to 60 percent "match rate" when the customer calls, Williams said, "much higher than we anticipated."

The computer will also "remember" a request that doesn't find a seller within 30 days so that members can be notified automatically as new sales offers come in, he said.

"We say we're not in competition with the other sources," said Solomon. "We don't purchase, stock or price parts."

Brokers, scrap dealers and speculators can't join the exchange, he added.

"The niches are out there," he said, "but finding one of your own is amazing."

Getting Source 2 ready to do business took a full year of "Kirk Jensen and me slugging it out," Solomon said.

"We were determined to start a major company, a market leader."

The idea of the surplus parts referral system didn't come up immediately, he added.

"From our previous experience, we had seen the problems of surplus parts — the brokers at work, the disposals," he said.

The question was whether that was a national experience or just a local experience, he added.

Solomon's last position was as design assurance manager for ESL in Sunnyvale, a subsidiary of Cleveland-based TRW. He worked with the electronic systems company five years.

Jensen, Source 2's systems vice president, was with ESL three years and was most recently its manager of data base administration.

The two built a computerized buyers' aid system there. It cross-referenced and verified part numbers.

Although the problems are similar, Jensen said, Source 2's programs and the approach to its programming was "completely different" from the previous project at ESL.

The Source 2 concept — and the extensive software development needed to implement it — was sound, apparently.

"We got major corporations (including Xerox, Exxon and Honeywell) on the exchange at the earliest point," Solomon said, "and we raised $2 million in nine weeks.

"Our feeling is that this showed that our homework was well done."

The software development was a data base management project, Williams explained. Programmers and analysts designed "a logical warehouse arranged as a giant physical warehouse would be," and a system to manage it.

Finding the right people is a big challenge

There are 125,000 kinds of integrated circuits and 350,000 kinds of capacitors, Solomon said. Source 2 researchers catalog each part by its characteristics — the kind of housing and leads it has, for example.

No previous reference material cross-referenced part data into substitute groups using full manufacturing part numbers, said Solomon.

Many large companies will do it, but only for the parts they use, he said. "We've arranged all the Japanese, Western European and U.S. parts into these groups."

Source 2's software increases the productivity of this cataloging with the help of a "menu," so that the workers just check off the part's characteristics, Williams said. They don't waste time typing in al' .e information.

. he software is the state of the art in data base management, said Solomon.

Traditionally, programmers are late in getting a job done, he said, and the Source II work was "incredibly complex.

"Ours said they would do it by April 1," he said, and even finished a little early. "There was a time when you couldn't get them to eat lunch," he added.

The system's hardware is also very sophisticated. Source 2 uses a Magnuson computer with a memory capacity that can expand to 50 billion bytes or units of information.

Computerworld magazine's last annual rating of computer users' satisfaction, conducted by Datapro Research Corp., ranked San Jose-based Magnuson Computer Systems' products first, ahead of those of IBM, Sperry Univac and Amdahl.

"We have several data 'dumps'," said Williams. Source 2 makes multiple copies of its inventory and requests at the end of the day, he said, and stores them in several locations.

The system could be working within 24 hours after any major unforeseen problem, he said.

Source 2's offices are connected by a microwave link and dedicated satellite, Williams said. A communications link lets the computer take all inquiries as they come in, no matter where they come from.

Marketing representatives don't need to bring prospective members into the local offices. They can call in and do a "play" search to see how the prospective member's current needs could be met through Source 2.

Buyers spend most of their time on the telephone, said Jensen, so this is an effective approach.

Many find what they've been trying to buy in the system, he said, and get impatient during the three- to four-day credit check that goes on before a company can trade on the exchange.

"We isolated 14 states that account for 90 percent of the electronics parts bought in the United States," Solomon said. "We determined that if we located in five cities, we could cover the 14 states."

Source 2 has offices in Irvine, Burlington, Mass., and Roseland, N.J., as well as the Santa Clara headquarters office. A Chicago office will open later this year; European and Far East offices are also in the works.

Source 2's field marketing representatives who work out of these regional offices are full-time employees, Solomon said.

The company hires people from the areas it serves, he said, because a personalized service relationship is important no matter how computerized a system is.

There are regional differences in personality, he said, and different working conditions. Members who call the exchange while there's a snowstorm in Boston should be talking to someone who can commiserate with them, for example.

There is a $50 billion market for electronic parts this year, according to Solomon.

Local suppliers fill roughly 25 percent of that market, he said. So Source 2 is working with part of a $12.5 billion (one-third of that United States) marketplace.

As with any start-up, Solomon said, finding the right people is a big challenge.

Traditionally, he said, sales representatives have been able to walk in, show a better transistor, and then sit back and adjust the price as sales of the part improve.

"We're literally pioneering an outrageously large concept," he said. "We're creating a new kind of marketplace.

"You can't borrow another company's training manual to teach a rep how to do this."

Source 2, in business eight months, has about 50 employees.

"We're operating with the Japanese organizational model," said Solomon, who "studied organizations formally" while working on a master's degree in management of technical companies at Stanford University.

"We don't differentiate by titles," he said. "We support each other in a team.

"Everyone has a gigantic chunk of responsibility — everyone is basically his or her own boss."

Every Source 2 employee has keys, he said, and no one, except the exchange operators, has set hours.

Source 2 uses the consensus approach to decision making, Solomon said. It takes longer to bring in solutions from many viewpoints, but when you do something, it's right.

Source 2 is a concept "as large as the New York Stock Exchange," Solomon said, with "member companies helping each other in a closed exchange.

"Members of the exchange will decide what to do next," Solomon said. What the exchange could carry wouldn't have to be limited to electronic parts.

"It's capitalism at its best, but democratized," he said of Source 2.

Members can be suspended for violating the exchange rules, he said, and the system can detect most cheating.

These standards and the exclusion of brokers, scrap dealers and speculators are simple principles of honesty, not elitism. They protect the Source 2 members, Solomon said.

"I think they may have a gold mine going, although this may be a bad time to enter the market," said Stu Dixon, materials manager for the Braegen Corp., Cupertino.

It costs a company a lot of money to do something with obsolete parts or excess quantities of current parts, he said.

Braegen has tried various methods in the past, he said — putting ads in Electronics News and "printing up listings and sending them to the major people in the area" among them.

"Now we spend some work on the listing," he said, but the rest of the search process goes through Source 2. The 10 percent charge, he said, "is very equitable."

As Source 2 is in business longer, prices on the exchange will probably stabilize, he suggested.

"The semiconductor industry is topsy-turvy now," he said.

"With some parts, you pay $8 six months ago and find they're $4 now," Dixon said. He attributes most of this kind of price drop to the depressed market, rather than to technological advances.

"The brokers seem to be out to make a fast buck," he said. "With Source 2, the people buying and selling are people like myself."

Source 2 is attractive because it offers members a no-risk deal, said Ed Basanese, purchasing manager for Avantek Inc. of Santa Clara. It "didn't come asking for money in advance or contracts to be signed."

Sellers can get better prices through Source 2 because buyers have specific needs for the parts, he said.

The buyers have a very good chance of finding extra parts from similar electronics companies through the system, he said.

Traditionally, people sell in large lots to brokers. The brokers make long lists of the parts that don't let a buyer know where they came from, or even if they were legally obtained. ■